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MUS FUNDING METHODOLOGY

A Report Prepared for the
Legislative Finance Committee
by

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Taryn Purdy
Senior Fiscal Analyst
September 28, 1992



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PURPOSE

In the January 1992 special session, the legislature reduced the fiscal 1992 general fund appropriation to the Montana University System (MUS) by \$2.2 million. Because a large part of the MUS appropriation is determined via a formula rather than incrementally (based on expenditures in fiscal 1992), the question arises: should special session reductions be reflected in the 1995 biennium current level budget presented to the 1993 legislature? The purpose of this report is to outline for committee review and comment the methodology that the Office of the Legislative Fiscal Analyst (LFA) plans to use in constructing the 1995 biennium current level budgets for the MUS. The report also provides a brief summary of the methodology the Office of Budget and Program Planning (OBPP) included in the budget instructions sent to the Office of the Commissioner of Higher Education (CHE) and CHE's instructions to the units for preparing their budget requests.

OVERVIEW OF CURRENT FUNDING METHODOLOGY

In recent biennia, the six university units and the five vocational-technical centers have been funded via a combination of a funding formula based upon enrollments and incremental funding, as shown in Table 1. The budgets of the

TABLE 1
Formula and Incremental Programs
Six University Units - Vo-Techs

<u>Formula Funded</u>	<u>Incrementally Funded</u>
Faculty Compensation*	Plant Operation & Maintenance
Support	Public Service+
Instructional Support*	Research+
Scholarships & Fellowships+	
Equipment++	
*Comprise the Instruction Program.	
+Six Units, only	
++Vo-Techs, only	

other agencies within the MUS (CHE, agricultural experiment station, cooperative extension service, forestry and conservation experiment station, bureau of mines, and fire services training school) are based on incremental funding.

Formula-funded programs comprised approximately 85 percent of the fiscal 1993 budget for the units as appropriated by the 1991 legislature.

The following table summarizes the formula used during the 1991 regular session to determine funding for the six university units and the formula factor values used to determine the budgets for fiscal 1993.

TABLE 2
Formula and Formula Factor Values - Six Units
Fiscal 1993

----- FACULTY COMPENSATION -----*							
<u>Unit</u>	<u>(Enrollment</u>	<u>÷</u>	<u>Student/Faculty</u> <u>Ratio)</u>	<u>x</u>	<u>Average</u> <u>Instructor</u> <u>(Salary</u>	<u>+</u>	<u>Benefits)</u>
MSU	9,457		16.88		\$37,441		21.070 %
UM	8,282		18.34		37,441		21.089 %
EMC	3,321		18.48		31,673		22.019 %
NMC	1,637		15.50		30,542		22.214 %
WMCUM	916		15.46		30,542		22.126 %
MCMST	1,523		15.91		37,441		21.058 %
----- SUPPORT -----**							
<u>Unit</u>	<u>Enrollment</u>	<u>x</u>	<u>Supp</u> <u>Fact</u>				
MSU	9,457		\$1,476				
UM	8,282		1,482				
EMC	3,321		1,549				
NMC	1,637		1,500				
WMCUM	916		1,634				
MCMST	1,523		1,833				
----- INSTRUCTIONAL SUPPORT -----							
<u>Unit</u>	<u>Enrollment</u>	<u>x</u>	<u>Instructional</u> <u>Support Factor</u>				
MSU	9,457		\$580				
UM	8,282		446				
EMC	3,321		351				
NMC	1,637		353				
WMCUM	916		386				
MCMST	1,523		736				

*Does not include supertuition

**Does not include modifications or audit expenses

For the 1993 biennium, scholarships and fellowships were calculated based on the actual percent of total tuition and fees represented by fee waivers in the previous year, applied against the total tuition and fees anticipated in the 1993 biennium, given current charges and enrollments.

The basic funding formulae used for the university units are also used to determine the budget for the vocational-technical centers, with the exception of the addition of a separate appropriation specifically for equipment purchases. The community colleges are funded via the formula illustrated in Table 3, which also shows the formula factor values used by the 1991 legislature.

TABLE 3
Formula and Formula Factor Values
Community Colleges*
Fiscal 1993

<u>Unit</u>	<u>Enrollment</u>	X	<u>Per Student</u> <u>Factor</u>	X	<u>General</u> <u>Fund</u> <u>Share</u>
Dawson CC	389		\$4,163		55%
Flathead Valley CC	987		4,163		55%
Miles CC	465		4,163		55%
*Does not include audit expenses					

Source of Funding Methodology

The overall methodology used to fund the six units in the past several biennia was recommended to the 1989 legislature by the University Funding Study Committee, a legislative committee established by the 1987 legislature. Enrollment was established as the average of the previous two years' actual enrollment. The remaining formula factor values currently in use are the factors initially derived

by the committee from actual expenditures in fiscal 1987, with adjustments by the 1989 legislature to move the factors closer to the peer levels, and by the 1991 legislature to fund specific additions, such as those deemed necessary to maintain accreditation in certain programs.

The methodology and specific formula factors used to fund the vo-techs were established by the 1991 legislature based upon the recommendations of the Postsecondary Education Study Committee (PESC) established by the 1989 legislature.

It is the prerogative of each legislature to determine how the six units, vo-techs, and community colleges will be funded and with what, if any, formula factors. Neither the overall methodology nor the specific factors are contained in statute. Consequently, the 1993 legislature will determine which, if any, formula factors are used to construct the budgets for the 1995 biennium.

The following sections: 1) discuss the LFA's planned methodology for determining the current level budget for the 1995 biennium for presentation to the 1993 legislature; and 2) contrast this methodology with OBPP budget instructions to the MUS and the instructions developed by CHE in response to the OBPP instructions. While the six units are used as the focus of discussion, many of the same issues apply to the vocational-technical centers and the community colleges.

PLANNED LFA FUNDING METHODOLOGY

Definition of LFA Current Level

Historically, the LFA current level is defined as the "level of funding required to maintain operations and services at the level authorized by the previous legislature, after adjustment for inflation." The LFA current level is not a recommendation. It is designed to provide a "benchmark" for the legislature in considering the Executive Budget and determining the appropriation level the legislature chooses to adopt.

LFA staff propose to use the formula factors used by the 1991 legislature to build the 1995 biennium current level budget for two primary reasons:

1) the factors currently in use were established by the 1991 legislature. The legislature did not make any adjustments to the formula in the January or July special sessions. Therefore, current legislative intent is contained in the current formula factors; and

2) the current level budgets of incrementally-funded agencies of state government do not automatically incorporate special session reductions. For example, if an agency made reductions exclusively in personal services (without actually eliminating FTE), none of these special session budget reductions will affect the 1995 biennium budget, as personal services are based upon a "point-in-time" snapshot of authorized FTE and salaries and benefits are calculated for the next biennium based upon the level in place at that time. Similarly, budget reductions made in equipment purchases in fiscal 1992 will not affect the 1995 biennium current level budget, since equipment is "zero-based". Thus, only

reductions in operating expenses made in fiscal 1992 will be carried forward into the next budget cycle.

Technical Adjustments

The LFA does plan to make two technical adjustments to the 1993 biennium formula factors:

- 1) incorporation of the salary and insurance increases contained in House Bill 509 in faculty compensation (salaries and benefits) and in the support and instructional support categories; and

- 2) application of an overall inflation factor to the instructional support and support formula factors.

Impact of LFA Current Level Definition

Using the formula factors used in the 1993 biennium will mean that reductions made to formula-funded programs as a result of the January special session will not carry forward into the 1995 biennium current level budget. In addition, this methodology will result in a larger 1995 biennium current level budget than the original 1993 biennium budget as appropriated by the 1991 legislature for three reasons:

- 1) an increase in enrollment at the six units of 1,321, or 5.3 percent;
- 2) an increase in personal services costs as a result of the pay plan approved by the 1991 legislature (House Bill 509); and
- 3) the application of the inflation factor.

Legislative Budget Issues

While the above methodology will be employed to determine the current level budget for the MUS, the 1993 legislature will no doubt consider many issues in determining the final appropriation to the MUS, including:

- 1) adjustment of any or all formula factors to adjust the total appropriation;
- 2) funding at a determined percentage of any or all formula factors; and/or
- 3) funding of any or all of the enrollment increases.

OBPP INSTRUCTIONS TO THE MUS

OBPP's instructions to the MUS for preparing and submitting its 1995 biennium budget request modify the formula by using actual expenditures and student faculty ratios (minus any additions made via budget amendment) in fiscal 1992, applied against the average of fiscal 1991 and 1992 actual enrollments, with a weighted inflation factor and/or specific additions for pay plan. The purpose of this modification of the formula is to carry into the 1995 biennium any adjustments in expenditures made in response to the January special session budget reductions.

OBPP has not determined the overall impact on the budgets of the six units and the vo-techs of these instructions.

CHE INSTRUCTIONS TO UNITS

CHE has issued instructions to all units of the MUS incorporating only a portion of the OBPP instructions for the formula-funded programs. The units are

using CHE' instructions in preparing their budget requests. CHE has taken exception to the OBPP budget instructions because the instructions: 1) exclude tuition and fee revenue added through budget amendment in fiscal 1992 due to increases in enrollment in the per student expenditure calculations; but 2) include the increased enrollment itself. Consequently, CHE has instructed the units to construct a budget based upon the fiscal 1993 formula factors as determined by the 1991 legislature, with addition of adjustments for pay plan, and incorporation of the OBPP weighted inflation factor, benefits percentages, and average faculty salaries. CHE has also instructed the units to apply a reduction factor of 1 percent to the resulting formula funded budgets to account for reductions made during the January special session.

SUMMARY EXAMPLE OF METHODOLOGIES

The following provides: 1) a summary of the three methodologies using the faculty compensation and support formula calculations for Montana State University as an example; and 2) a general overview of the potential impacts of each. Please note that the figures are estimates, as several of the factors have not yet been precisely calculated or determined.

Faculty Compensation

The following table shows the formula factors that would be used to determine faculty compensation. As shown, there are two differences among the methodologies: 1) student faculty ratios; and 2) the CHE reduction factor.

TABLE 4
Faculty Compensation - Formula Factors
1995 Biennium

--- FORMULA FACTORS ---

<u>Methodology</u>	<u>Enrollment</u>	<u>St/Fac Ratio</u>	<u>Avg. Salaries</u>	<u>Benefits</u>	<u>Reduction Factor</u>
Executive	9,574	18.15	\$39,625	21.291 %	0 %
CHE	9,574	16.88	39,625	21.291 %	1 %
Proposed LFA	9,574	16.88	39,625	21.291 % *	0 %

----- CALCULATION -----

<u>Totals</u>	<u>Total</u>	<u>With Reduction Factor</u>	<u>Over (Under) Exec</u>	<u>Over (Under) HB2 FY93**</u>
Executive	\$22,937,283	\$25,354,779	--	(\$41,198)
CHE	27,259,559	26,986,964	--	1,590,987
Proposed LFA	27,259,559	27,259,559	--	1,863,582

*Precise benefit calculation not yet made.

**Does not include supertuition, as appropriated by the 1991 legislature.

As the table shows, using the OBPP methodology could result in a higher student/faculty ratio, with a corresponding reduction in budget, compared to the current formula factor levels. While the reduction resulting from OBPP's methodology is relatively small (\$41,178) compared to the fiscal 1993 House Bill 2 appropriation, note that the calculation includes higher salaries than were used to determine the 1993 appropriation due to additions for the pay plan. If comparable salaries had been used, the reduction would have been significantly larger.

According to OBPP, using the actual student/faculty ratios and actual instructional support expenditure per student should result in a budget (prior to additions for pay plan or inflation) that approximates actual expenditures per student in fiscal 1992 for the instruction budget as a whole. However, OBPP has not precisely defined the formula factor values or calculated the overall impact of the instructions on either the faculty compensation or instructional support budgets.

How OBPP defines the formula factor values will have a major impact on the formula and the resulting current level budget.

The CHE and LFA methodologies both provide for an increase in funding over the fiscal 1993 level as appropriated by the 1991 legislature due to the increased enrollment and higher pay. The 1 percent reduction factor included in the CHE instructions totals approximately \$275,000.

Support

Table 5 provides an estimate of the overall impact of the various support formula methodologies. As shown, the OBPP methodology (actual fiscal 1992 expenditures for the support program, minus budget amendments and audit costs) may result in higher formula costs than the LFA or CHE methodologies because actual expenditures in the support program were higher than anticipated during the 1993 biennium appropriation process.

In all three methodologies adjustments are made for the pay plan and budget modifications (library books, Regents' Employee Reporting System, and student minimum wage) that were added manually by the 1991 legislature rather than included in the factor. Since fiscal 1992 pay plan costs are already incorporated in OBPP's calculated support rate (Column #1), a \$50 per student (3.2 percent) increase was added to the OBPP calculation to account for increased fiscal 1993 pay plan costs in the 1995 biennium (Column #2). The CHE and proposed LFA calculations include the increased costs of the pay plan for the full biennium of approximately \$113 per student (Column #2). Since the OBPP methodology already incorporates budget modifications, no additional funds are added. Both the CHE

and LFA methodologies add in these costs (Column #3). All three methodologies provide an overall increase in funding from the fiscal 1993 level as appropriated by the 1991 legislature due to the addition of the 1993 biennium budget modifications and the full biennium pay plan costs.

No inflation factor was used in this table, as it has not yet been calculated by OBPP, CHE, or the LFA. However, as in the past, the LFA current level calculation will include an inflation factor, based upon the inflation factors agreed upon by OBPP and LFA for state agencies. CHE and OBPP also plan to use a weighted inflation factor.

TABLE 5
Support - Formula Factors
1995 Biennium

----- FORMULA FACTORS -----							
<u>Office</u>	<u>Enrollment</u>	<u>Support Rate*</u>	<u>Pay Plan Adjustment**</u>	<u>Modification Adjustment</u>	<u>Total Support Rate</u>	<u>Inflation Factor***</u>	<u>Reduction Factor</u>
		#1	#2	#3	#4		
Executive	9,574	\$1,582	\$50	\$0	\$1,632	---	0%
CHE	9,574	1,476	113	28	1,617	---	1%
Proposed LFA	9,574	1,476	113	28	1,617	---	0%
<u>Totals</u>							

----- CALCULATION -----

	<u>With Reduction Factor</u>	<u>Over (Under) Exec</u>	<u>Over (Under) HB2 FY93****</u>
Executive	\$15,620,293	--	\$1,752,683
CHE	15,322,346	(297,947)	1,454,736
Proposed LFA	15,477,117	(143,176)	1,609,507

*Does not include audit costs.

**Precise calculation not yet made.

***Inflation factor not yet established primarily assumed to be uniform.

****Does not include audit costs. All appropriated by the 1991 legislature.

Instructional Support

OBPP, CHE, and the LFA will all use the methodologies shown in Table 2 to calculate instructional support. Since the methodology used to determine which expenditures constitute instructional support is not precisely specified in the OBPP instructions, no comparative calculation has been made. However, budgets will increase over the 1993 biennium level with both the CHE and LFA methodology due to the increases in enrollments and pay.

Scholarships and Fellowships

OBPP's instructions for calculating scholarships and fellowships use the same methodology used in the 1993 biennium, which will also be employed in the LFA current level calculations. Therefore, the resulting current level budgets should be equal. Scholarships and fellowships will increase due to the increase in enrollments and higher tuition and fee charges.

Incremental Programs

Incrementally-funded program budgets will be prepared by OBPP, CHE, and the LFA using the same methodology (actual fiscal 1992 expenditures, adjusted for inflation and other factors) employed in the 1993 biennium.

Summary

Due to the expression of legislative intent inherent in the current formula factors and because special session budget reductions will not necessarily be

incorporated into the budgets of other state agencies, the LFA current level budgets for the MUS will be determined using current formula factor values as developed by the 1991 legislature, with adjustments for inflation and the pay plan approved by the 1991 legislature. Although the precise impact has not yet been calculated, this methodology will result in higher current level budgets than appropriated in the 1991 biennium due to an increase in enrollments and the pay plan. OBPP has instructed the MUS to calculate its budget request using actual fiscal 1992 expenditures per student and student faculty ratios, applied against actual fiscal 1991 and 1992 student FTE enrollments, with additions for inflation and pay plan. The financial impact on the MUS budget request of these instructions has not yet been determined, primarily because OBPP has not yet defined and calculated the precise formula factor values. CHE has instructed the units to submit budgets based upon the 1991 biennium formula factor values, with adjustments for pay plan and inflation, as well as a budget reduction factor of 1 percent. While the overall impact of CHE's instruction has also not been calculated, it will result in a higher budget request for the 1995 biennium than the current biennium appropriation, due to higher enrollment and the pay plan.

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